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No. 87-633

IN THE

Supreme Court of the United States

OCTOBER TERM, 1987

APEX OIL COMPANY,

Petitioner,

—against—

JOSEPH DiMAURO, et al.,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION OF RESPONDENT NEW YORK MERCANTILE EXCHANGE

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 701-3000

Counsel of Record for Respondent New York Mercantile Exchange

Of Counsel:

CAHILL GORDON & REINDEL
(a partnership including
professional corporations)
PETER LEIGHT
KATHY SILBERTHAU STROM

November 16, 1987

QUESTIONS PRESENTED

1. Whether the court of appeals erred in applying the rule of its 1984 decisions in *Sam Wong & Son, Inc.* v. *New York Mercantile Exchange* and *Ryder Energy Distribution Corp.* v. *Merrill Lynch Commodities Inc.* (not cited in the petition) that the bad faith standard for contract market liability under the Commodity Exchange Act requires that the sole or dominant reason for the contract market's action or inaction be ulterior motive or self interest?

2. Whether the court of appeals erred in finding on the facts that there was not even "slight evidence" linking the contract market defendants to any antitrust conspiracy?

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BRIEF IN OPPOSITION OF RESPONDENT NEW YORK MERCANTILE EXCHANGE

Respondent New York Mercantile Exchange ("Exchange")[1] respectfully requests that the Court deny the petition of Petitioner Apex Oil Company ("Apex") that a writ of certiorari issue to review the decision and judgment of the United States Court of Appeals for the Second Circuit, entered on June 17, 1987, which affirmed the judgment of the United States District Court for the Southern District of New York, granting the motion of the Exchange for summary judgment dismissing Apex's complaint against it.

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1 Pursuant to Rule 28.1, the Exchange advises the Court that the Exchange is a not-for-profit corporation having no parents, subsidiaries, or affiliates.

STATEMENT OF THE CASE

This action exists because Apex chose not to liquidate its short position of approximately 4400 February 1982 futures contracts (for delivery of roughly 184 million gallons of heating oil) before trading in the contract ended on the Exchange. Apex chose not to liquidate its short position although Apex was not in a position to deliver in accordance with the Rules of the Exchange. (Pet. App. at A43, A46).[2]

Apex had placed itself in a predicament akin to that described by Daniel Drew in the last century: "He who sells what isn't his'n must buy it back or go to prison."

The Exchange is a designated contract market on which its clearing members on behalf of themselves and customers enter into contracts to make ("short") or take ("long") future delivery of various commodities. Apex's clearing member was Goldman Sachs & Co. ("Goldman Sachs").

The Exchange is a self-regulatory body. It adopts Rules establishing the terms of contracts traded on the Exchange, Commodity Exchange Act ("CEA") § 5a(12), 7 U.S.C. § 7a(12) (1982); CFTC Reg. 1.41, 17 C.F.R. § 1.41 (1987).

The Exchange is itself closely regulated by the Commodity Futures Trading Commission ("CFTC"). All contract and trading Rules must be approved by the CFTC, CEA § 5a(12), 7 U.S.C. § 7a(12) (1982). The Exchange may not enforce unapproved Rules; once approved, the Exchange must enforce and may not revoke Rules, CEA § 5a(8) and (12), 7 U.S.C. § 7a(8) and (12) (1982); CFTC Reg. 1.53, 17 C.F.R. § 1.53 (1987).

Apex's complaint is that the Exchange did not help Apex out of the predicament of its own making in February 1982—that

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2 The following abbreviations are used in this brief: "Pet. ___" for citation to the Petition for a Writ of Certiorari, "Pet. App. ___" for citation to the Appendix to the Petition, and "A ___" for citations to the Joint Appendix filed with the court of appeals.

the Exchange did not take emergency action. Apex contends that the Exchange should have altered its delivery Rules to permit Apex to deliver, as the amended complaint put it, "reasonably over the course of the delivery month" (A 767), rather than in accordance with Exchange Rules.

Apex had no oil at GATX, the facility it had designated for delivery. (Pet. App. at A50). Apex made false representations to the Exchange concerning the amount of oil it had (and would have) at GATX. (Pet. App. at A50). Instead of changing the Rules, the Exchange "jawboned" clearing members representing the longs, who were to take delivery, and Apex, the short who was to make delivery. (Pet. App. at A103). The Exchange met with representatives of Apex and the longs. (Pet. App. at A12, A50). It discussed ways of resolving the delivery problem and urged flexibility. It did not change the Rules which it was bound to enforce absent emergency action. It reminded Goldman Sachs, the short clearing member acting for Apex, of the penalties for delinquency and default in the event of a failure to deliver. As a result of the efforts of the Exchange there was no default. (Pet. App. at A13, A51). The Exchange enforced its Rules. Apex, which had no oil, bought oil and the delivery problem was resolved.

The district court, in a detailed and careful opinion, ruled that there was no evidence of bad faith or of participation by the Exchange in a conspiracy and granted summary judgment dismissing all claims against the Exchange. (Pet. App. at A96-A108). The court of appeals affirmed, stating that:

> "Apex failed to present evidence tending to show that the Exchange acted or failed to act as a result of self interest or bad faith as interpreted in a number of this court's decisions. *See, e.g., Brawer* v. *Options Clearing Corp.*, 807 F.2d 297 (2d Cir. 1986); *Sam Wong & Son* v. *New York Mercantile Exchange*, 735 F.2d 653 (2d Cir. 1984)."

(Pet. App. at A35).

For a complete statement of the case, the Court is respectfully referred to the decision of the court of appeals (Pet. App. at A7-A13) and the decision of the district court (Pet. App. at A42-A51, A96-A101).[3]

REASONS FOR DENYING THE PETITION

I. The Decisions of the Court of Appeals Concerning the Meaning of the "Bad Faith" Standard Are Correct, Are Not The Subject of Conflicting Decisions and Do Not Warrant Review by the Court

A. There is No Conflict Among the "Federal Courts"

The bad faith standard of liability applicable to a commodity exchange is well established, and, contrary to Apex's assertions, there is no conflict among the federal courts of appeals concerning it. The petition does not present any question worthy of review by this Court. *See* Supreme Court Rule 17.

Two decisions of the United States Court of Appeals for the Second Circuit, the more recent of which is not even cited by Apex, establish that bad faith governs all claims addressed to the regulatory conduct of commodity exchanges ("contract

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3 There are numerous misstatements in Apex's statement of the case. For example, Apex asserts, without citation, that there was "full knowledge of that conspiracy on the part of the exchange defendants." (Pet. at 6 n.7). To the contrary, the district court found "insufficient probative evidence . . . that the exchange defendants knew of any such conspiracy" (Pet. App. at A103), and that finding was sustained by the court of appeals.

Another example is Apex's misleading description of the Rules of the Exchange and the parties' obligations thereunder. (Pet. at 7-8). While the parties were allowed to "work out" changes in dates, times and places for delivery, the Rules state the requirements for delivery absent such consensual changes. A long had the right to nominate the date of delivery. Absent an agreement, the short was obliged to deliver on that date. The district court and the court of appeals so found. (Pet. App. at A10, A47-A48).

markets" designated as such by the CFTC under the CEA). A cause of action does not lie against an exchange unless "self-interest or other ulterior motive unrelated to proper regulatory concerns" is the "sole or the dominant reason" for the action or inaction in question. *Sam Wong & Son, Inc.* v. *New York Mercantile Exchange*, 735 F.2d 653, 677 (2d Cir. 1984) ("*Sam Wong*"); *Ryder Energy Distribution Corp.* v. *Merrill Lynch Commodities Inc.*, 748 F.2d 774 (2d Cir. 1984) ("*Ryder Energy*"). Judge Meskill's opinion for the Second Circuit in *Ryder Energy* stated the rule as follows:

> "A claim of bad faith must be supported by two allegations: first, that the exchange acted or failed to act with knowledge; *and* second, that the exchange's action or inaction was the result of an ulterior motive. *Sam Wong*, 735 F.2d at 671; *Miller* v. *New York Produce Exchange*, 550 F.2d 762, 766-67 (2d Cir.), *cert. denied*, 434 U.S. 823 . . . (1977)."

(*Ryder Energy*, *supra*, 748 F.2d at 780, emphasis added).

Apex, not even citing *Ryder Energy*, incorrectly argues that bad faith is established "where an exchange knows of a manipulation but fails to take any action to prevent it." (Pet. at 15). In addition to the *Ryder Energy* decision, the construction for which Apex argues was urged upon and rejected by the Court of Appeals for the Second Circuit in *Sam Wong*. Judge Friendly's opinion for the court there makes clear that the same standard applies to both exchange action and inaction: "[A] plaintiff . . . [will] have the initial burden of showing that ulterior motive, *e.g.*, financial gain or personal animosity was 'a substantial or motivating factor' in the *taking of or failure to take action*." 735 F.2d at 677 (emphasis added; citations omitted).

In *Ryder Energy*, the Second Circuit, citing *Sam Wong*, reiterated that "[w]e have recently made it clear that the bad faith requirement governs claims of both exchange action and inaction." 748 F.2d at 780. In *Ryder Energy*, plaintiff alleged the Exchange knew that clearing members were violating Ex-

change rules and failed to enforce them (as is argued by Apex here).[4]

Apex has not shown why the Court should review the rule of the court of appeals on the bad faith standard. In urging a different standard Apex relies upon inapposite or superseded decisions decided before the court of appeals decisions in *Sam Wong* and *Ryder Energy*,[5] and a brief filed by the CFTC with the Court of Appeals for the Seventh Circuit. (Pet. at 19).[6]

Apex also cites *Baird* v. *Franklin*, 141 F.2d 238 (2d Cir.), *cert. denied*, 323 U.S. 737 (1944) ("*Baird*"), a case involving a claim against the stock exchange based on broker misconduct,

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4 The February 1982 delivery problem shows exactly why alleged knowledge alone is not sufficient. If the Exchange knew that the longs were conspiring (it did not) and also knew that Apex violated the Rules by not having oil to deliver (it did not know this until late on February 5), it would have faced a delivery problem and two wrongdoers. In this situation, the Exchange must have discretion to enforce the delivery Rules and then discipline the wrongdoers. The fact that the Exchange first enforces the Rules and then addresses the wrongdoers should not be a basis for liability. The Exchange, as *Ryder Energy* squarely held, may act in good faith with knowledge of wrongdoing so long as it acts honestly and in the interest of the market.

5 All of the district court cases cited by Apex (Pet. at 19 & n.14) were decided before the decisions in *Sam Wong* and *Ryder Energy*. To the extent that any of those decisions applied a standard of negligence or differing standards to govern exchange action and inaction, such decisions have been overruled by *Ryder Energy* and *Sam Wong*.

6 The only other authority cited by Apex, *Deaktor* v. *L.D. Schreiber & Co.*, 479 F.2d 529 (7th Cir.), *rev'd per curiam sub nom. Chicago Mercantile Exchange* v. *Deaktor*, 414 U.S. 113 (1973), does not even address the standard of liability. As that court stated: "[t]he sole issue in these appeals is whether the district court could take jurisdiction of these actions or whether the Commodity Exchange Commission properly has primary jurisdiction over these proceedings." 479 F.2d at 531. While letting stand a negligence claim, the decision includes no discussion whatsoever of the standard of liability because that issue was not before the court.

and its progeny,[7] to attempt support its assertion that the courts of appeals are in conflict on the question of whether bad faith can be shown by exchange inaction.[8] The court of appeals has recently declined to follow *Baird* and has held that the bad faith standard of liability governs private actions against securities exchanges, *Brawer* v. *Options Clearing Corp.*, 807 F.2d 297 (2d Cir. 1986), *cert. denied*, 56 U.S.L.W. 3243 (U.S. Oct. 5, 1987) (No. 86-1825) ("*Brawer*"), relying upon decisions holding that bad faith is the standard of liability in actions against commodity exchanges and upon the 1982 codification of the bad faith standard in section 22(b)(4) of the CEA, 7 U.S.C. § 25(b)(4) (1982).[9]

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7 *Hochfelder* v. *Midwest Stock Exchange*, 503 F.2d 364 (7th Cir.), *cert. denied*, 419 U.S. 875 (1974); *Marbury Management, Inc.* v. *Alfred Kohn, Wood, Walker & Co.*, 373 F. Supp. 140 (S.D.N.Y. 1974).

8 In *Baird*, the court of appeals held that the stock exchange was required to enforce its rules requiring disciplinary action. However, *Baird* is inapposite since it involved construction of a written agreement between the stock exchange and the Securities and Exchange Commission ("SEC") required by former § 6(a)(1) of the Securities Exchange Act of 1934 as a condition to registration. 15 U.S.C. § 78f(a)(1)(1940). 141 F.2d at 242. No such provision governed or governs commodity exchanges.

In any event, as Justice Harlan once stated:

> "[C]ontrary decisions between different panels of the same Court of Appeals will not be considered to present a reviewable conflict, since such differences of view are deemed an intramural matter to be resolved by the Court of Appeals itself."

J.M. Harlan, *Manning the Dikes*, 13 A.B.C.N.Y. Record 541, 552 (1958). *See also* Supreme Court Rule 17.

9 Section 22(b)(4) reads as follows:

> "A person seeking to enforce liability [for failure of an exchange to enforce a rule or for enforcement of a rule] must establish that the contract market, licensed board of trade, clearing organization, registered futures association, officer, director, governor, committee member, or employee acted in bad faith in failing to take action or in taking such action as was taken, and that such failure or action caused the loss."

This clause applies to Mr. Raber, the Exchange's Vice-Chairman in 1982, as an officer and governor of the Exchange.

The *Brawer* ruling applied the bad faith standard to a self-regulatory body's decision not to adjust an option price to the consequent disadvantage of option writers and the advantage of option holders. The instant case presents another instance of discretionary exchange decision-making—action or inaction—to the disadvantage of a short required, but unable, to make delivery and (it was alleged) to the advantage of longs required and entitled to take delivery.

Finally, Apex's citation (Pet. at 15, 19) of a CFTC Brief filed in a case which, according to the CFTC, does not involve discretionary exchange response to a market crisis—but rather involves exchange responsibility for an elaborate scheme to defraud investors orchestrated by one of its members—further underscores the absence of conflicting courts of appeals authority on the definition of bad faith. (Pet. at 15).

B. The Courts Below Correctly Applied the Bad Faith Standard.

The court of appeals and the district court correctly concluded that there was no self interest, nor ulterior motive and therefore no bad faith. (Pet. App. at A35, A102). Apex does not allege that the Exchange had any personal interest in the February deliveries or any bias toward any participant in the deliveries. The Exchange acted to address a delivery problem (A 2622) that would not have occurred if Apex had been in a position to deliver.

As stated by the district court, "Apex's true quarrel with the Exchange is that it failed to interpret the rules as Apex would have liked. This does not raise an issue of bad faith." (Pet. App. at A105).

C. Petitioner's First Question Has Been Addressed by Congress

As Apex recognizes, Congress in 1982 amended the CEA to expressly provide that "bad faith" must be shown to state a claim against a contract market, CEA § 22(b)(4), 7 U.S.C.

§ 25(b)(4).[10] While this case arises prior to the codification of the bad faith standard, the existence of the amended statute highlights that there is no "special and important" reason for this Court to consider the question. Supreme Court Rule 17.

II. The Summary Judgment Dismissal of an Antitrust Claim by the District Court Affirmed by the Court of Appeals, Even Under the "Slight Evidence" Concept of That Court, Does Not Warrant Review By This Court

Apex cannot transform what is essentially its disagreement with findings of fact into a legal issue by contending that the court of appeals misapplied the Court's decision in *Monsanto Co.* v. *Spray-Rite Service Corp.*, 465 U.S. 752 (1984), in affirming the district court's summary judgment decision. Contrary to Apex's contention, the court of appeals explicitly applied its "slight evidence" rule in deciding whether the Exchange (or any other defendant) was connected to the conspiracy. (Pet. App. at A28, A32-A33).

> "We have carefully reviewed this evidence and, while we reverse and remand as to the antitrust claims against Belcher for the reasons stated above, *and remain aware that " 'once a conspiracy is shown, only slight evidence is needed to link another defendant with it,' " Wilkinson, supra*,[11] *since we do not find such a link*, we conclude that affirmance of the grant of summary judgment is appropriate as to the remaining defendants."

(Pet. App. at A28) (emphasis added).

While under the "slight evidence" concept of the court of appeals, a lesser showing may be required to connect (the Exchange does not accept the correctness of this concept) a particular defendant to a conspiracy than is necessary to

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10 *Sam Wong* held that the bad faith standard applies to pre-1982 causes of action.

11 *United States* v. *Wilkinson*, 754 F.2d 1427, 1436 (2d Cir.), *cert. denied*, 472 U.S. 1019 (1985) (*quoting United States* v. *Marrapese*, 486 F.2d 918, 921 (2d Cir. 1973), *cert. denied*, 415 U.S. 994 (1974)).

establish the existence of a conspiracy in the first instance, it does not abrogate the requirement that to survive a motion for summary judgment plaintiff must present probative evidence that a particular defendant was linked or connected to the conspiracy.[12] The court of appeals, after a careful review of the district court's decision and the record, concluded that there was no credible evidence from which "plausible" inferences could be drawn linking the Exchange to any antitrust conspiracy. (Pet. App. at A33). In making this inquiry, it is clearly appropriate to evaluate the probity of particular circumstantial evidence in light of the *Monsanto* "tends to exclude" evidentiary standard. Apex's attempt to argue (Pet. at 23) that, against the backdrop of a conspiracy, any use of the *Monsanto* analysis constitutes an "unsupportable extension" of the decision defies common sense. Apex is in fact merely quibbling with the lower courts' findings of fact.[13] That is not an appropriate matter for review by this Court.

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12 *See, e.g.*, *United States* v. *Wardy*, 777 F.2d 101, 107 (2d Cir. 1985), *cert. denied*, 475 U.S. 1053 (1986) ("[H]owever slight or circumstantial, the evidence must tend to prove that the appellants did enter into some form of agreement.").

13 Apex's argument that it has been deprived of its Seventh Amendment right to a trial by jury is without merit. Where summary judgment has been properly granted (as here), no right to jury trial is denied. *Tull* v. *United States*, 107 S. Ct. 1831, 1836 (1987); *Celotex Corp.* v. *Catrett*, 106 S. Ct. 2548, 2555 (1986).

CONCLUSION

The petition for a writ of certiorari should be denied.

November 16, 1987

Respectfully submitted,

WILLIAM E. HEGARTY
80 Pine Street
New York, New York 10005
(212) 701-3000

Counsel of Record for Respondent New York Mercantile Exchange

Of Counsel:

CAHILL GORDON & REINDEL
(a partnership including
professional corporations)
PETER LEIGHT
KATHY SILBERTHAU STROM